

## Message Text

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ACTION SS-25

INFO OCT-01 ISO-00 SSO-00 /026 W  
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FM AMEMBASSY LISBON

TO SECSTATE WASHDC IMMEDIATE 8637

C O N F I D E N T I A L LISBON 6580

EXDIS

FOR THE SECRETARY AND HARTMAN

E.O. 11652: GDS

TAGS: PFOR, ECON, PO

SUBJECT: USG LOAN FOR PORTUGAL. FOURTH AND SIX ON  
THE TWENTY

1. WE HAVE AGAIN REACHED A POINT IN PORTUGAL WHERE WE  
NEED YOUR PERSONAL ASSISTANCE.

2. LAST JUNE YOU ASKED WHAT MORE I NEEDED TO DO THE JOB.  
I SAID A LIQUIDITY LOAN IN THE NEIGHBORHOOD OF \$300  
MILLION. YOU TOOK THIS UP WITH BILL SIMON AND ARTHUR  
BURNS. ARTHUR WAS HIGHLY FAVORABLE AND BILL AGREED IN  
PRINCIPLE IF THE SOCIALISTS, ONCE IN OFFICE, FOLLOWED  
SOUND ECONOMIC POLICIES.

3. TREASURY HAS NOW COMPLETED ITS STUDY OF SOARES'  
ECONOMIC POLICY. WHILE I HAVE NOT SEEN THE REPORT, I  
DOUBT THEY WILL ARGUE WITH THE FUNDAMENTAL THRUST OF  
HIS POLICY, ALTHOUGH THEY MAY DIFFER ON TECHNICALITIES  
AND TIMING. THIS GOVERNMENT HAS ANNOUNCED AND/OR TAKEN  
A SERIES OF HIGHLY POSITIVE STEPS, NOTABLY IN  
AGRARIAN REFORM, LABOR, AND CONSUMER SUBSIDY AREAS.  
EVEN ACCELERATED IMPLEMENTATION OF THIS PROGRAM, HOW-  
EVER, IS UNLIKELY TO AVOID EXHAUSTING PORTUGAL'S  
LIQUIDITY RESERVES. PORTUGAL THUS FACES THE POSSIBILITY  
OF A SHARP UNPROGRAMMED CUT IN DOMESTIC CONSUMPTION  
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THAT WOULD ACCENTUATE UNEMPLOYMENT, INFLATION, AND

ECONOMIC DISLOCATION. THE RESULTING POLITICAL OPPOSITION COULD WELL TOPPLE THE NATION'S FRAGILE POLITICAL STRUCTURE. HAVING COME FROM OUR OWN GOAL LINE TO THE OPPOSITION'S 20, IT WOULD BE A SHAME TO LOSE THE BALLGAME AT THIS POINT.

4. THE POLITICAL CASE FOR A USG LOAN SEEMS TO ME TO BE OVERWHELMING.

-- AFTER TEETERING ON THE BRINK, PORTUGAL HAS CONVINCINGLY DEMONSTRATED ITS DESIRE TO RETURN TO THE WESTERN FOLD. PRESIDENT FORD PROMISED FULL SUPPORT TO THE MODERATES IF THEY TURNED THE SITUATION AROUND, AND THEY HAVE.

-- A NEW, POPULARLY ELECTED PRESIDENT AND DEMOCRATIC GOVERNMENT ARE IN PLACE AND ARE GRAPPLING WITH THE COUNTRY'S PROBLEMS. THE COMMUNISTS AND THEIR COLLABORATORS ARE OUT OF KEY POSITIONS NOT JUST IN THE GOVERNMENT BUT IN THE MILITARY AS WELL.

-- A FULL HOUSECLEANING IS UNDERWAY IN EDUCATION AND A SMALLER ONE IN THE MEDIA; THE SOCIALISTS ARE MANEUVERING TO BREAK THE COMMUNIST GRIP ON ORGANIZED LABOR; AND AN ALL-OUT ASSAULT IS BEING LAUNCHED ON THE COMMUNIST AGRICULTURAL STRONGHOLD IN THE ALENTEJO.

-- SOARES HAS COME TO TRUST US, AND HE RESPONDS WELL TO OUR CONCERNS. DESPITE PUBLIC CRITICISM AND OPPOSITION WITHIN HIS PARTY, HE HAS TAKEN A STRONG PRO-EUROPEAN STAND, REJECTED STRIDENT COMMUNIST OVERTURES FOR A COALITION, AND PUBLICLY SINGLED OUT THE UNITED STATES AS A COUNTRY WITH WHICH PORTUGAL SHOULD DEVELOP A SPECIAL RELATIONSHIP.

-- A STABLE, DEMOCRATIC AND ECONOMICALLY STRONG PORTUGAL CAN SERVE AS A DRAMATIC EXAMPLE TO DEMOCRATIC FORCES IN THE REST OF EUROPE. A FAILURE AT THIS POINT WOULD BE A MAJOR SETBACK.

5. SOARES' ABILITY TO CARRY ALL THIS OFF DEPENDS ON HIS CAPACITY TO DEAL WITH THE ECONOMIC SITUATION. IF WE DO NOT PROVIDE HIM WITH THE FINANCIAL FLEXIBILITY TO KEY HIS ECONOMIC MOVES TO POLITICAL REALITIES, THE OUTLOOK IS PRECARIOUS.  
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-- AN AUTHORITARIAN RIGHT WING COULD MOVE IN, FORCING A POLARIZATION. THE DEMOCRATS WOULD ONCE AGAIN JOIN A REJUNVENATED COMMUNIST PARTY IN OPPOSITION, EUROPEAN SUPPORT WOULD DRY UP, AND THE STAGE WOULD BE SET FOR A REPETITION OF THE 1974-75 SCENARIO.

-- A COALITION GOVERNMENT MIGHT GAIN A FEW MONTHS BUT WOULD SOLVE NONE OF THE BASIC PROBLEMS. IN

ADDITION, IT WOULD SUFFER FROM INTERNAL DISSENSION, FORFEIT LABOR TO THE COMMUNISTS, AND BECOME INCREASINGLY DEPENDENT ON MILITARY BACKING. A COALITION IS PROBABLY DESIRABLE SOME TIME NEXT YEAR, BUT IT MUST BE BORN OUT OF CONFIDENCE, NOT OUT OF DESPERATION. -- A GOVERNMENT OF NATIONAL SALVATION WOULD INCLUDE COMMUNISTS AND TAKE US RIGHT BACK TO THE FRUSTRATING COSTA GOMES DAYS.

6. SOARES' ACTIONS ON THE ECONOMIC FRONT ARE LIMITED BY WHAT THE POLITICAL MARKET WILL BEAR. IN FOUR MONTHS HE WILL BE MUCH STRONGER, BUT RIGHT NOW INSISTENCE ON SOLVING EVERY ECONOMIC PROBLEM AT ONCE COULD BRING HIM DOWN. HE IS TAKING ON FRAMERS, CONSUMERS, AND THE COMMUNISTS -- ALL AT THE SAME TIME. WE NEED TO LET HIM CALL THE TACTICAL SHOTS -- AND RIGHT NOW HE IS PUSHING HIS POLITICAL MANDATE TO ITS LIMIT.

7. THE 300 MILLION DOLLARS MAY REPRESENT THE ADDITIONAL PUSH SOARES NEEDS TO GET OVER THE IMMEDIATE POLITICAL HURDLES. IT WOULD CLEARLY SIGNIFY OUR MORAL AND FINANCIAL COMMITMENT TO PORTUGAL'S INTEGRATION INTO THE WESTERN WORLD. IT WOULD PROVIDE PORTUGAL AN OPPORTUNITY TO CONSOLIDATE ITS FLEDGLING DEMOCRATIC INSTITUTIONS, TO IMPLEMENT NEEDED ECONOMIC REFORMS, AND TO OBTAIN INTERNATIONAL FINANCING FOR THE LONGER TERM. WHILE I CAN'T GUARANTEE SUCCESS, OF COURSE, IT SEEMS TO ME THAT THE USG HAS AN OPPORTUNITY FOR SIGNIFICANT POLITICAL GAIN AT LITTLE COST. I WOULD HOPE THEREFORE THAT YOU COULD AGAIN INTERVENE WITH SECRETARY SIMON AND CHAIRMAN BURNS IN ORDER TO ARRANGE THE REQUESTED \$300 MILLION

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DOLLAR LOAN FOR PORTUGAL.  
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## Message Attributes

**Automatic Decaptioning:** Z  
**Capture Date:** 01 JAN 1994  
**Channel Indicators:** n/a  
**Current Classification:** UNCLASSIFIED  
**Concepts:** POLICIES, FOREIGN ASSISTANCE, LOANS  
**Control Number:** n/a  
**Copy:** SINGLE  
**Draft Date:** 24 SEP 1976  
**Decaption Date:** 28 MAY 2004  
**Decaption Note:** 25 YEAR REVIEW  
**Disposition Action:** RELEASED  
**Disposition Approved on Date:**  
**Disposition Authority:** CunninFX  
**Disposition Case Number:** n/a  
**Disposition Comment:** 25 YEAR REVIEW  
**Disposition Date:** 28 MAY 2004  
**Disposition Event:**  
**Disposition History:** n/a  
**Disposition Reason:**  
**Disposition Remarks:**  
**Document Number:** 1976LISBON06580  
**Document Source:** CORE  
**Document Unique ID:** 00  
**Drafter:** n/a  
**Enclosure:** n/a  
**Executive Order:** GS  
**Errors:** N/A  
**Film Number:** D760361-0582  
**From:** LISBON  
**Handling Restrictions:** n/a  
**Image Path:**  
**ISecure:** 1  
**Legacy Key:** link1976/newtext/t19760924/aaaaatxb.tel  
**Line Count:** 156  
**Locator:** TEXT ON-LINE, ON MICROFILM  
**Office:** ACTION SS  
**Original Classification:** CONFIDENTIAL  
**Original Handling Restrictions:** EXDIS  
**Original Previous Classification:** n/a  
**Original Previous Handling Restrictions:** n/a  
**Page Count:** 3  
**Previous Channel Indicators:** n/a  
**Previous Classification:** CONFIDENTIAL  
**Previous Handling Restrictions:** EXDIS  
**Reference:** n/a  
**Review Action:** RELEASED, APPROVED  
**Review Authority:** CunninFX  
**Review Comment:** n/a  
**Review Content Flags:**  
**Review Date:** 04 MAY 2004  
**Review Event:**  
**Review Exemptions:** n/a  
**Review History:** RELEASED <04 MAY 2004 by BoyleJA>; APPROVED <30 AUG 2004 by CunninFX>  
**Review Markings:**

Margaret P. Grafeld  
Declassified/Released  
US Department of State  
EO Systematic Review  
04 MAY 2006

**Review Media Identifier:**  
**Review Referrals:** n/a  
**Review Release Date:** n/a  
**Review Release Event:** n/a  
**Review Transfer Date:**  
**Review Withdrawn Fields:** n/a  
**Secure:** OPEN  
**Status:** NATIVE  
**Subject:** USG LOAN FOR PORTUGAL. FOURTH AND SIX ON THE TWENTY  
**TAGS:** PFOR, ECON, PO, US  
**To:** STATE  
**Type:** TE  
**Markings:** Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 04 MAY 2006